FILE COPY

OCT 12 1946
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM, 1946.

Nos. 42, 43.

In the Matter

of

AMERICAN FUEL & POWER COMPANY,
INLAND GAS CORPORATION,
KENTUCKY FUEL GAS CORPORATION,
Debtors.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,

—against—

LOUIS A. GREEN and ROBERT HEILBRUNN, Known in these Proceedings as the GREEN COMMITTEE and MORRIS GREEN,
Respondents.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,

—against—

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, JACK PATTON and P. G. MEADOR,
Respondents.

BRIEF FOR RESPONDENTS GREEN COMMITTEE AND MORRIS GREEN.

OSCAR S. ROSNER,
Counsel for Respondents, Green Committee and Morris Green.

BAKER, OBERMEIER, ROSNER & ROSENSON,
Attorneys for Respondents, Green Committee and Morris Green.

OSCAR S. ROSNER,
Of Counsel.

JAY RAYMOND LEVINSON,
On the Brief.

INDEX.

	PAGE
Opinions Below	1
Jurisdiction	2
Statement of Case	2
Summary of Argument	4
Argument:	
I. The federal court sitting in a bankruptcy case in Kentucky should apply the conflict of laws rules of Kentucky in determining the validity of a contract	4
A. The validity of the provision for interest on interest was governed initially by State law	4
B. The principles of the decision rejecting the doctrine of a substantive common law for the federal courts are here applicable	5
C. These principles rejecting the old doctrine of federal courts' common law apply to Conflict of Laws cases in Bankruptcy	9
D. The Choice of Law Rule enunciated in *Seeman* v. *Philadelphia Warehouse Company* has no application to this case	12
II. Under the conflict of laws rule of Kentucky the local law of New York as to the validity of a provision for interest on interest is controlling	15
A. The Kentucky conflict of laws rule refers to New York as the source of the governing law	15

PAGE

B. The Kentucky conflict of laws rule in referring to New York requires the application of the New York local law against interest on interest 17

C. The conflict of laws rule of New York would call for the use of the local law of New York in this case 18

III. The considered determination by the Circuit Court of Appeals of the interest on interest question, predicated upon decisions of the New York Court of Appeals, should not be overruled 20

Conclusion 22

TABLE OF CASES CITED:

Bingham v. *United States*, 296 U. S. 211 16

Clearfield Trust Co. v. *United States*, 318 U. S. 363 ... 11

Commonwealth Farm Loan Co. v. *Caudle*, 203 Ky. 761, 263 S. W. 24 15

Continental Securities Co. v. *N. Y. C. & H. R. R. Co.*, 217 N. Y. 119 ..... 20, 21

Corn Exchange Bank v. *Klauder*, 318 U. S. 434 13

Curtis v. *Leavitt*, 15 N. Y. 9 19

De Wolfe v. *Johnson*, 10 Wheat. 383 ..... 14, 15

D'Oench, Duhme & Co. v. *Federal Deposit Insurance Corporation*, 315 U. S. 447 (1943) 11

Erie Railroad Co. v. *Tompkins*, 304 U. S. 64, 6, 7, 9, 10, 11, 43

Griffin v. *McCoach*, 313 U. S. 498 (1941) 9

Guaranty Trust Co. v. *York*, 326 U. S. 99 (1945) 7, 9

Heiser v. *Woodruff*, 66 S. Ct. 853 (1946) 12

Hiscock v. *Varick Bank of New York*, 206 U. S. 28 4, 5

PAGE

Holley v. *Talcott*, 129 App. Div. 233 (1st Dept., 1908) 18
Holmberg v. *Armbrecht*, 66 S. Ct. 582 (1946) 11
Huddleston v. *Dwyer*, 322 U. S. 232 ..... 17, 21, 22

Klaxon v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941) 5, 8, 9

Lann v. *United Steel Works Corp.*, 166 Misc. 465, 1 N. Y. S. 2d 951 13
Liebeskind v. *Mexican Light & Power Co.*, 116 F. 2d 971 13

McKenzie, Trustee in Bankruptcy v. *Irving Trust Co.*, 323 U. S. 365 (1945) 11
Mooly v. *Barker*, 188 Ky. 401 ..... 15, 16

Newburger-Morris Co. v. *Talcott*, 219 N. Y. 505 21

Palmer v. *Hoffman*, 318 U. S. 109 (1943) 9
Pan-American Securities Corp. v. *Krup Actiengesellschaft*, 169 Misc. 445, 6 N. Y. S. 2d 993, Affd. 256 App. Div. 955, 10 N. Y. S. 2d 205 13
Pensacola & A. R. Co. v. *Hilton's Trustee*, 147 Ky. 553, 144 S. W. 1077 ..... 15, 16

Rex Coat Co. v. *Campbell*, 213 Ky. 636 16
Russell v. *Todd*, 309 U. S. 280 9

Seeman v. *Philadelphia Warehouse Company*, 274 U. S. 403 ..... 12, 13, 14
Swift v. *Tyson*, 16 Pet. 1 5

United States v. *Mitchell*, 271 U. S. 9 16

Webster v. *Fall*, 266 U. S. 507 16
Westchester Mortgage Co. v. *Grand Rapids and Ionia Railroad Co.*, 246 N. Y. 194 ..... 18, 19
William Glenny Glass Co. v. *Taylor*, 99 Ky. 24, 34 S. W. 711 ..... 15, 16

OTHER AUTHORITIES CITED:

	PAGE
Bankruptcy Act, as amended:	
Section 24 (c), 11 U. S. C. Sec. 47(c)	2
Section 60-a	11
Section 77B	2
Chapter X	2, 3
Beale, Conflict of Laws (1935), Secs. 7.3, 8.1	18
Goodrich, Conflict of Laws (2d ed., 1938), p. 12	18
Judicial Code, as amended by the Act of February 13, 1925, Section 240(a), 28 U. S. C. Sec. 347 (a)	2
Restatement, Conflict of Laws:	
Sec. 7	18
Sec. 8	18
Sec. 356	13, 17

Supreme Court of the United States

OCTOBER TERM, 1946.

Nos. 42, 43.

In the Matter

of

AMERICAN FUEL & POWER COMPANY,
INLAND GAS CORPORATION,
KENTUCKY FUEL GAS CORPORATION,
Debtors.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,

—against—

LOUIS A. GREEN and ROBERT HEILBRUNN, Known in these Proceedings as the GREEN COMMITTEE and MORRIS GREEN,
Respondents.

VANSTON BONDHOLDERS PROTECTIVE COMMITTEE,
Petitioner,

—against—

CARL B. EARLY, DANIEL MATTHEWS, THOMAS MATTHEWS, JACK PATTON and P. G. MEADOR,
Respondents.

BRIEF FOR RESPONDENTS GREEN COMMITTEE AND MORRIS GREEN.

Opinions Below.

The District Court rendered no opinion but indicated the reasons for its decision during the argument (R. 56). An order and judgment setting forth the findings of fact and conclusions of law were thereupon entered (R. 192). The opinion of the Circuit Court of Appeals is reported in 151 F. (2d) 479, and is also reprinted at R. 214 *et seq.*

Jurisdiction.

The judgments of the Circuit Court of Appeals were entered on October 9, 1945 (R. 213). Rehearing was denied on November 26, 1945 (R. 241). The petition for writs of certiorari of the Vanston Bondholders Protective Committee (Oct. Term, 1945, Nos. 848 and 849) was filed on February 14, 1946, and the petition for certiorari of the Van Horn Bondholders Protective Committee (Oct. Term, 1945, Nos. 850 and 851), on February 15, 1946. Writs of certiorari were granted on March 25, 1946. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, 28 U. S. C. Sec. 347(a), and Section 24(c) of the Bankruptcy Act, as amended, 11 U. S. C. Sec. 47(c).

Statement of Case.

On December 1, 1930 a bill of complaint was filed by Williams and Gibson, plaintiffs, against Inland Gas Corporation, defendant (hereinafter called "Inland"), in the District Court of the United States, Eastern District of Kentucky, alleging diversity of citizenship as the basis of jurisdiction, and praying for the appointment of a receiver in equity of Inland (R. 101). Upon such bill of complaint an order was made and filed December 2, 1930 appointing W. E. Lockhart, Receiver of Inland (R. 113). The equity receivership was continued until October 26, 1935, when an order was entered appointing a temporary trustee in reorganization proceedings under Section 77B of the Bankruptcy Act, which was followed by an order, filed November 23, 1935, making permanent the appointment of such trustee. The provisions of Chapter X of

the Bankruptcy Act were subsequently made applicable to these proceedings (R. 191).

Through the indenture trustees, Chatham Phenix National Bank and Trust Company and James F. McNamara, Inland paid in the City and State of New York, where said trustees maintained their office, the semi-annual interest coupons on its first mortgage bonds until it defaulted on the semi-annual interest coupon due February 1, 1931 (R. 187). On April 3, 1931 the indenture trustees declared the entire principal due and payable pursuant to the acceleration provisions of the indenture. This was followed by a bill of foreclosure filed by the indenture trustees on April 14, 1931.

Petitioner is a committee of first mortgage bondholders of Inland. The indenture, or deed of trust, securing the first mortgage bonds, was executed in the State of New York. The bonds and the interest coupons thereto attached were also executed and issued in that State; and were payable at the office of the indenture trustee, or, at the option of the bearer, in Illinois. There is no evidence of record that any bondholder demanded payment in Illinois. Nor do the proofs of claim filed by the bondholders indicate that any coupons had been detached from the bonds or negotiated to third parties (R. 219).

Petitioner seeks to enforce a clause in the indenture, or deed of trust, providing for interest on interest, the validity of which provision is the matter in dispute between petitioner and other creditors of Inland.

The District Court, without rendering an opinion, decided that the provision for interest on interest was valid under New York Law (R. 56). The Circuit Court of Appeals reversed this decision, holding such a provision to be invalid under New York Law (R. 213).

Summary of Argument.

1. The Federal Court sitting in a bankruptcy case in Kentucky should apply the conflict of laws rules of Kentucky in determining the validity of a contract.

2. Under the conflict of laws rules of Kentucky the local law of New York as to the validity of a provision for interest on interest is controlling.

3. The considered determination by the Circuit Court of Appeals of the interest on interest question, predicated upon decisions of the New York Court of Appeals, should not be overruled.

ARGUMENT.

I.

The Federal Court sitting in a bankruptcy case in Kentucky should apply the conflict of laws rules of Kentucky in determining the validity of a contract.

A. The Validity of the Provision for Interest on Interest Was Governed Initially by State Law.

The contract in question was governed in its inception by State law. Neither the Bankruptcy Law nor any other Federal law applied to the contract when made. The Bankruptcy Law does not assume to change the substantive rights and duties of the creditors and the bankrupt. It leaves these to the determination of State law. In *Hiscock* v. *Varick Bank of New York*, 206 U. S. 28, 38, a bankruptcy case, this Court said:

"The questions of the extent and validity of the

pledge were local questions, and the decisions of the courts of New York are to be followed by this court."

If, therefore, the whole loan contract was made in Kentucky, a Federal Court sitting in Kentucky would undoubtedly use Kentucky law, whether the Federal Court were sitting in a diversity of citizenship case or in a bankruptcy case.

And when the contract, as here, is made in one State (New York) and its validity is being determined in a bankruptcy proceeding pending in another State (Kentucky), the determination is still governed by State law, according to State conflict of law principles, for the Federal Court has no power to apply a special law to an occurrence merely because it is a conflict of laws case. So, if this case were in a Kentucky State Court, the Kentucky conflict of laws rules would apply. If it were in the Federal Court in Kentucky on the grounds of diversity of citizenship, the same State law would apply. (*Klaxon* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941).

Now that the case happens to be in the Federal court on the bankruptcy side, the normal rights of the parties should not be distorted by this accident of forum. The contention of the petitioner is that there should be this alteration of the rights of the parties by the use of a special choice of law rule of the federal courts, only when there is a conflict of laws case in bankruptcy in the Federal court. The recent cases of this Court, it is believed, reject such a conclusion.

B. The Principles of the Decision Rejecting the Doctrine of a Substantive Common Law for the Federal Courts Are Here Applicable.

The old doctrine of *Swift* v. *Tyson*, 16 Pet. 1, was that there was a special body of common law for the federal

courts, different from that which would be applied to the same cases in the State courts. It is this whole doctrine of a special body of substantive law for the federal courts which this Court rejected in *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64.

The opinion of the Court in the *Tompkins* case was not confined in its reasoning to diversity of citizenship cases. As a preliminary, it is true, Justice Brandeis does discuss the Rule of Decisions Act and shows it had been misconstrued in the past. But this misconstruction was expressly stated not to be the ground of the decision, the Court stating:

> "If only a question of statutory construction were involved, we should not be prepared to abandon a doctrine so widely applied throughout nearly a century" (304 U. S. p. 77).

The Court placed the decision on a principal ground which is equally applicable to the Federal Court sitting in Bankruptcy. This ground is that in this country the law applicable to a case is State law, except where the Constitution or Federal Statutes otherwise provide:

> "Except in matters governed by the Federal Constitution or by acts of Congress, the law to be applied in any case is the law of the state . . . Congress has no power to declare substantive rules of common law applicable in a state . . . And no clause in the Constitution purports to confer such a power upon the federal courts." (304 U. S. p. 78.)

There were two other grounds of the *Tompkins* decision, which are also present in the principal case. One was the rejection of the old jurisprudential theory of law as a "brooding omnipresence," on which Mr. Justice Holmes had led the attack. In rejecting this view of law, the

Tompkins decision was not confined to the mere diversity of citizenship situation which gave rise to it. As Mr. Justice Frankfurter has put it:

> "In overruling *Swift* v. *Tyson*, 16 Pet. 1, *Erie R. Co.* v. *Tompkins* did not merely overrule a venerable case. It overruled a particular way of looking at law which dominated the judicial process long after its inadequacies had been laid bare." (*Guaranty Trust Co.* v. *York*, 326 U. S. 99, 101 (1945).)

Another supporting ground of the *Tompkins* decision was the condemnation of the evils which flowed from the existence of two bodies of law within a single State, one applicable in the State courts, the other in the Federal courts:

> "It made rights enjoyed under the unwritten 'general law' vary according to whether enforcement was sought in the state or in the federal court: . . . Thus, the doctrine rendered impossible equal protection of the law. In attempting to promote uniformity of law throughout the United States, the doctrine had prevented uniformity in the administration of the law of the state." (304 U. S. p. 74.)

These grounds apply with full force here. There are many insolvents who work out their difficulties in State court proceedings or by out-of-court adjustments based on the rights under the applicable State laws. If the determination of the validity and extent of creditors' rights under State law were to be supplanted by a special body of Federal courts' law once a debtor got into bankruptcy, it would bring the same confusion and shopping for a forum which this Court decried.

It will readily be granted by the respondents that the view they urge will not achieve uniformity of law in all

courts, for the law of Kentucky may be different from the law of New York. But the diversities thus produced are the inevitable results of our Federal system, and the existence of these diversities from State to State is assumed and in a measure dealt with by the Federal Constitution as in the full faith and credit clause and the privilege and immunities clause. The existence of such diversities gives no support to the opposing course which would attempt to create uniformity of result in all Federal Courts in Bankruptcy at the cost of diversity between State and Federal Courts in the same State. Mr. Justice Reed states the matter cogently in *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941), a case which also involved a controversy over interest in a conflict of laws case:

> "Any other ruling would do violence to the principle of uniformity within a state upon which the *Tompkins* decision is based. Whatever lack of uniformity this may produce between federal courts in different states is attributable to our federal system, which leaves to a state, within the limits permitted by the Constitution, the right to pursue local policies diverging from those of its neighbors. It is not for the federal courts to thwart such local policies by enforcing an independent 'general law' of conflict of laws" (p. 496).

It might be argued that it would be more convenient to the Federal Courts in Bankruptcy and to the Securities and Exchange Commission to administer a single law as to interest or a single law of conflict of laws. Their convenience, however, must give way before the Constitutional requirements for the application of State law in these matters.

C. These Principles Rejecting the Old Doctrine of Federal Courts' Common Law Apply to Conflict of Laws Cases in Bankruptcy.

The existing diversity in the conflict of laws rules of the various states may cause the result to vary with the forum State whose conflict of laws rules are to be used. This, too, is one of the results of our federal system. And this Court has adhered to the policy of the *Tompkins* decision in just such cases and has consistently and unanimously held that the conflicts of laws rules of the forum should be applied. It so held when the question was whether the award of interest after judgment was one of "procedure" governed by the law of the forum or a matter of "substance" governed by the law of the occurrence (*Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U. S. 487 (1941); when the question was one of choice of the governing law of a contract and of public policy (*Griffin* v. *McCoach*, 313 U. S. 498 (1941); and again when the question was as to the burden of establishing contributory negligence (*Palmer* v. *Hoffman*, 318 U. S. 109 (1943).)

There have been repeated efforts to confine the *Tompkins* decision to its facts. This Court, however, has steadily followed the policies underlying the *Tompkins* decision as guide and has given them sweeping application. So it rejected the contention, as already shown, that the principle should not apply in conflict of laws. It first raised the question whether in administering equitable remedies this principle should apply (*Russell* v. *Todd*, 309 U. S. 280, 294); and it then held that in such situations, too, it should apply (*Guaranty Trust Co. of New York* v. *York*, 326 U. S. 99). In the last-mentioned case, involving a statute of limitations, the opinion of

Mr. Justice Frankfurter discusses the guiding policies in the *Tompkins* opinion and then states the question:

> ". . . in the aspect that alone is relevant to our problem, namely, does it significantly affect the result of a litigation for a federal court to disregard a law of a State that would be controlling in an action upon the same claim by the same parties in a State court" (326 U. S. 99, 109).

The petitioner cites several recent cases in which this Court did not apply the law of the State. When these cases are examined, particularly in the light of the various possible sources of rules to which the Federal courts might go, they support, it is believed, the views urged in this brief.

There are three possible choice of law rules which are the subject of argument here. The one, which the respondents urge, is the law of the State in which the court is sitting, Kentucky. The second, which the petitioner contends for, is a special body of law which the petitioner urges should be adopted for the Federal Courts in Bankruptcy. The third is a national law, the law of the land, which would bind all courts alike, Federal and State. It is this last source of law which is employed in the non-diversity cases relied on by the petitioner.

The national law as the governing law may have various foundations, as the decisions of this Court have shown. The activities of the Federal Government and of its instrumentalities may be governed by a law which as to those activities is "the law of the land" and must be used in all courts in which those activities come in issue. So in a suit by the Federal Deposit Insurance Corporation on a right given to it by the implications of a Federal statute, it was held that the law of the State should not

be used (*D'Oench, Duhme & Co.* v. *Federal Deposit Insurance Corporation,* 315 U. S. 447 (1943)). And in a suit by the United States involving a check drawn by the Treasurer of the United States, again the law of the state was not applied (*Clearfield Trust Co.* v. *United States,* 318 U. S. 363).

Similarly, where there is a cause of action arising under a federal statute, it is for the national law to determine the applicable time limitation. In *Holmberg* v. *Armbrecht,* 66 S. Ct. 582 (1946), this principle was applied in a suit to enforce a liability created by the Federal Farm Loan Act.

These cases did not turn on the difference between diversity jurisdiction and non-diversity jurisdiction. Nor did they in any sense involve the use of a special law for the federal courts or for the bankruptcy side of the federal courts. They all involved the application of the law of the land, that is, a national law applicable to determine the rights of the parties in whatever court they may be questioned. The position of the petitioner, it will be remembered, is that there should be a special rule of conflict of laws for the federal courts sitting in bankruptcy, which will be used to determine the validity and extent of the contract rights of private parties. The petitioner's view, if adopted, would again bring to pass the harmful effects pointed out in the *Tompkins* case.

The discussion by Chief Justice Stone in a note to his opinion in *McKenzie, Trustee in Bankruptcy* v. *Irving Trust Co.,* 323 U. S. 365, 371, footnote 2 (1945), is of no aid to the petitioner. The *McKenzie* case involved a problem of preference under Sec. 60-a of the Bankruptcy Act, and held that state standards which control the effectiveness of a transfer likewise determine the precise

time when a transfer is deemed to have been made or perfected. Surely, there is no more reason for the bankruptcy court to devise its own conflict of laws rules for the determination of the validity of claims before it than there would be for it to devise its own standards to control the effectiveness of a transfer or to provide rules for the determination of rights and duties under private contract law or sales law.

In the same way, the opinion of the late Chief Justice in *Heiser* v. *Woodruff*, 66 S. Ct. 853, 855-6 (1946), relied on by the petitioner, is inapplicable here. All that this Court decided in the *Heiser* case was that in passing upon and rejecting or allowing the proof of claim in the case, the court of bankruptcy proceeds—not without appropriate regard for rights acquired under state law—under federal statutes which govern the proof and allowance of claims based on judgments. There was no question of the validity of a contract involved in that case.

D. The Choice of Law Rule Enunciated in Seeman v. Philadelphia Warehouse Company Has No Application to This Case.

The deed of trust, securing the Inland first mortgage bonds, was executed in the State of New York. The bonds and the interest coupons thereto attached were also executed and issued in that State; and were payable there, at the office of the indenture trustee, or, at the option of the bearer, in Illinois. There is no evidence of record that any bondholder demanded payment in Illinois. Nor do the proofs of claim filed by the bondholders indicate that any coupons have been detached from the bonds or negotiated to third parties (R. 219).

The petitioner seeks to avoid the reference to New York

law, by relying upon the case of *Seeman* v. *Philadelphia Warehouse Company*, 274 U. S. 403.

Although it is our contention that the rule of the *Seeman* case is in no event applicable here since the decision of the *Tompkins case* (footnote 8, opinion of Mr. Justice Jackson, *Corn Exchange Bank* v. *Klauder*, 318 U. S. 434, 437), we further urge that the *Seeman* case is distinguishable from the instant case on its facts.

As we have already seen, New York was the place of contracting and the primary place of performance in the case at bar. In fact, it was the only place of actual performance. The option to receive payment in Illinois never having been exercised, no valid argument may be predicated upon the hypothetical situation that might have arisen if such option had been exercised. (Restatement Conflict of Laws, Sec. 356; *Liebeskind* v. *Mexican Light & Power Co.*, 116 F. 2d, 971, 973; *Lann* v. *United Steel Works Corp.*, 166 Misc. 465, 1 N. Y. S. 2d, 951; *Pan-American Securities Corp.* v. *Krupp Actiengesellschaft*, 169 Misc. 445, 451, 6 N. Y. S. 2d, 993, Affd. 256 App. Div. 955, 10 N. Y. S. 2d, 205.) In the *Seeman* case, on the other hand, there was no question that repayment was stipulated to be made in Pennsylvania.

Moreover, the crux of the *Seeman* decision is that Pennsylvania, in addition to the fact that it was the agreed place of repayment, possessed a substantial relationship to the transaction. Holding there that the "effect of the qualification is merely to prevent the evasion or avoidance at will of the usury law otherwise applicable, by the parties' entering into the contract or stipulating for its performance at a place which has no normal relation to the transaction and to whose law they would not otherwise be subject," this Court went on to emphasize that the lender in that case "organized and con-

ducting its business in Pennsylvania, was subject to the laws of that state and had a legitimate interest in seeking their benefit."

But in the instant case, the record discloses that all the parties to the Deed of Trust were located in New York, except the debtor, which in any event had no office and carried on no business in Illinois. Hence, Illinois was a place which had "no normal relation to the transaction and to whose law they would not otherwise be subject."

Alternatively, the petitioner argues that the *Seeman* case is authority for a choice of law rule which would make Kentucky law the source of jurisprudence governing the case at bar, because the mortgaged property is situated there. The fallacy in this contention is twofold. First, in the *Seeman* case Pennsylvania was the stipulated place of repayment, while in the instant case Kentucky was not the stipulated place of repayment. Second, it has been expressly held by this Court that the *lex loci contractus* must govern in a question of usury, although the debt is secured by a mortgage on real property in another state. In *De Wolfe* v. *Johnson,* 10 Wheat. 383, this Court said:

> "With regard to the locality of the contract of 1815, we have no doubt that it must be governed by the law of Rhode Island. The proof is positive that it was entered into there, and there is nothing that can raise a question but the circumstance of its making a part of the contract that it should be secured by conveyances of Kentucky land. But the point is established, that the mere taking of foreign security does not alter the locality of the contract with regard to the legal interest. Taking foreign security does not necessarily draw after it the consequence that the contract is to be fulfilled where the security is taken. The legal fulfillment of a contract of loan,

on the part of the borrower, is repayment of the money, and the security given is but the means of securing what he has contracted for, which, in the eye of the law, is to pay where he borrows, unless another place of payment be expressly designated by the contract."

II.

Under the conflict of laws rule of Kentucky the local law of New York as to the validity of a provision for interest on interest is controlling.

A. The Kentucky Conflict of Laws Rule Refers to New York as the Source of the Governing Law.

In *Moody* v. *Barker*, 188 Ky. 401, 403, the Court of Appeals of Kentucky declared:

> "It may be stated without exception that if under the *lex loci contractus* the contract for any reason is void, it will be invalid everywhere, and will not be enforced by the *lex fori*, although it would be valid if executed in that jurisdiction."

The petitioner cites *Commonwealth Farm Loan Co.* v. *Caudle*, 203 Ky. 761, 263 S. W. 24; *William Glenny Glass Co.* v. *Taylor*, 99 Ky. 24, 34 S. W. 711, and *Pensacola & A. R. Co.* v. *Hilton's Trustee*, 147 Ky. 553, 144 S. W. 1077, as announcing a contrary rule, but a reading of those cases readily discloses that they do not justify the interpretation placed upon them by petitioner. In the *Commonwealth Farm Loan Company* case, *supra*, the Court stated that it *might* apply a rule that where notes are executed in one state and payable in another, the parties may lawfully contract for the highest legal rate of interest permissible by the laws of either state. However,

it did not apply such a rule in that case. Consequently that case cannot be accepted as modifying to any extent the rule laid down in the *Moody* case above cited.

In the case of *William Glenny Glass Company* v. *Taylor, supra,* the note involved was void under New York law, but valid under Kentucky law. The Court found as a fact, and any other finding would have been unjustified, that the note was executed in Kentucky and hence, under the Kentucky rule, its validity was determined under Kentucky law, even though payable in New York.

Pensacola & A. R. Co. v. *Hilton's Trustee, supra,* is inapplicable. The question here presented was neither raised nor considered by the Court. Questions that merely lurk in a record, but which are neither brought to the attention of the Court nor ruled upon' are not to be considered as having been so decided as to constitute precedents. (*Webster* v. *Fall,* 266 U. S. 507; *United States* v. *Mitchell,* 271 U. S. 9; *Bingham* v. *United States,* 296 U. S. 211; *Rex Coat Co.* v. *Campbell,* 213 Ky. 636.)

The suggestion by the petitioner that the Kentucky courts would use any bona fide contact with any State whose local law would uphold the interest provision is not sustained by any Kentucky decisions cited by petitioner.

New York was here the place of making of the contract; the place of performance thereof; and the place where the indenture trustee and the individual trustee were located. New York is the State of overwhelmingly dominant connections with the contract. New York, therefore, is the place whose law is to govern. Two other places are suggested by the petitioner, Illinois and Kentucky.

Illinois is suggested because it was a place of possible payment. The bonds provided that they would be paid in

New York, "or, at the option of the bearer or such registered owner" in Illinois. The record fails to disclose that any of the bondholders have demanded payment be made to them in Illinois, and in the absence of such a demand the place of payment is that provided in the bond, New York. (Restatement Conflict of Laws, Sec. 356.)

Kentucky is suggested by the petitioner because the property under the mortgage was in Kentucky. No Kentucky authority is cited by the petitioner to support this suggestion, and none seems to exist.

Moreover, the Circuit Court of Appeals having based its decision as to the Kentucky choice of law rule upon the determinations of the highest courts of the State, it should not be disturbed (*Huddleston* v. *Dwyer*, 322 U. S. 232, 237).

B. The Kentucky Conflict of Laws Rule in Referring to New York Requires the Application of the New York Local Law against Interest on Interest.

When Kentucky refers to New York as the State whose law should apply, it naturally refers to the ordinary or local law of New York. So in this case it would use the New York law against interest on interest.

It is argued, however, by the petitioner, first, that Kentucky in referring to New York should apply the New York rule of conflict of laws and should follow where it leads, and, second, that New York has a different conflict of laws rule from that which the respondents believe Kentucky has, and that the New York rule would use the Kentucky or Illinois law.

The first of these arguments calls for the adoption of the doctrine of the *renvoi*. No Kentucky authority is cited in support of the use of the *renvoi*, and none seems to exist. There is little support in any American state

for the *renvoi*. Judge Goodrich in his treatise writes: "The theory of *renvoi* has been the subject of much legal discussion, most of which has condemned its application in all but a few situations" (Goodrich, Conflict of Laws (2d ed., 1938), p. 12). The Restatement of Conflict of Laws condemns the use of the *renvoi* except in matters of divorce and of title to land (Restatement, Conflict of Laws, Secs. 7, 8, discussed in Beale, Conflict of Laws (1935), Secs. 7.3, 8.1).

C. The Conflict of Laws Rule of New York Would Call for the Use of the Local Law of New York in This Case.

The Conflict of Laws rule of New York is to be considered in this case only if this Court believes the doctrine of *renvoi* would be used by the Kentucky court, a conclusion which the preceding subdivision of the brief shows is not the fact.

In New York, the leading case on the subject of applicable choice is *Holley* v. *Talcott*, 129 App. Div. 233 (1st Dept., 1908), where it was held that the interpretation and validity of a contract for the loan of money is to be determined by the law of the place where the contract was made. The Court decided, therefore, that since the agreement to loan money took place in New York, the contract was a New York contract though the notes evidencing the transaction were signed and made payable in Pennsylvania, and the question as to whether it was usurious must be determined by the laws of New York, not by that of Pennsylvania.

Nothing to the contrary was held in *Westchester Mortgage Co.* v. *Grand Rapids and Ionia Railroad Co.*, 246 N. Y. 194, cited by the petitioner, for it is clearly dis-

tinguishable on its facts. As was there stated (per Lehman, *J.*):

> "Unquestionably the note is usurious if it was made in the State of New York, and is governed by the laws of this State. The Appellate Division has made findings and conclusions to the effect that the note was made and delivered in Rhode Island, and its validity must be determined by the laws of that State" (p. 197).

Distinguishable, too, as involving a contract made elsewhere than in the State of New York, is the case of *Curtis* v. *Leavitt*, 15 N. Y. 9, upon which the petitioner relies. At page 227 of the opinion there we find the following:

> "The documentary and oral evidence shows that the contract for the sale of these bonds was made and the money advanced on them paid in England; that the semi-annual interest to accrue thereon was to be paid in London, and the principal ultimately to be repaid there. . . . These facts make the contract an English contract; and the question of usury, therefore, is to be determined by the English law."

Even if the petitioner were correct as to the extraordinary liberality of the New York courts in the conflict of laws field as to usury, the doctrine would not apply here. The favorable conflict of laws doctrines in alleged usurious transactions arose to prevent the severe provisions for penalties and forfeiture in cases of usury. The usury prohibitions are statutory, and the court had to deal with their harsh effects as well as it could. But the New York rule against interest on interest involved here is neither a law against usury nor is it a legislative command with harsh sanctions. The New York rule is not a prohibition of usury, but a refusal to enforce a

covenant for interest on interest. It is a prohibition, not imposed by statute, but developed by the New York courts to strike down these provisions for interest on interest after maturity which would consume the debtor's assets and would gravely prejudice other creditors whose claims did not contain such a provision. Surely, the New York courts which created and developed this rule to prevent injustice will not now develop and apply a rule of conflict of laws for the purpose of doing away with this protection. Since New York is certainly the State of the most numerous and most important contacts in this case, it is clear that its courts would not apply a conflict of laws rule that the law of any State having any contact with the transaction may be used for the purpose of escaping the very protection which those same courts have developed.

III.

The considered determination by the Circuit Court of Appeals of the interest on interest question, predicated upon decisions of the New York Court of Appeals, should not be overruled.

The Circuit Court of Appeals in the instant case correctly ascertained the law of New York to be that a covenant made prior to the accrual of interest, to pay interest on interest, is contrary to the public policy of the State and is, therefore, unenforceable.

Relied upon by the Circuit Court of Appeals, among other cases, were two opinions of Judge Cardozo, writing for the Court, in *Continental Securities Co.* v. *N. Y. C. & H. R. Co.*, 217 N. Y. 119, 125:

"It makes no difference that the promise to pay

interest is represented by coupons. Until detached and separately negotiated, a coupon is merely an incident of the bond without greater force than any other promise for the payment of interest. (*Williamsburgh Savings Bank* v. *Town of Solon*, 136 N. Y. 465, 481.)"

And in *Newburger-Morris Co.* v. *Talcott*, 219 N. Y. 505, 510:

"The charge of compound interest was correctly disallowed. The rule is settled that a promise to pay interest upon interest is void if made at a time before simple interest has accrued. (*Young* v. *Hill*, 67 N. Y. 162.) The provision in the contract that interest shall be 'charged on the account current. . . . at the rate of 6 per cent per annum,' must, therefore, mean simple interest. Any other promise, made at the outset of the dealings would be invalid."

After reviewing the New York authorities on the question of interest on interest, the opinion of the Court below in the instant case concludes (R. 226):

"We have found no guidance to decision save in the opinions of the highest court of New York. Upon our rounded view of the opinions of that tribunal, we have concluded that the district court erred in holding that the non-negotiated coupons attached to the first mortgage bonds of the Inland Gas Corporation bear simple interest, at the rate provided in the mortgage, from the respective due dates of the coupons until paid."

In *Huddleston* v. *Dwyer*, 322 U. S. 232, 237, this Court said:

"The decision of the highest court of a state on matters of state law are in general conclusive upon us,

and ordinarily we accept and therefore do not review, save in exceptional cases, the considered determination of questions of state law by the intermediate federal appellate courts, Cf. *Ruhlin* v. *New York Life Ins. Co., supra.*"

Hence, we respectfully urge that such a considered determination of State law by the Circuit Court of Appeals should not be disturbed.

CONCLUSION.

It is respectfully submitted that the judgments of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

OSCAR S. ROSNER,
Counsel for Respondents,
Green Committee and Morris Green.

BAKER, OBERMEIER, ROSNER & ROSENSON,
Attorneys for Respondents,
Green Committee and Morris Green.

OSCAR S. ROSNER,
Of Counsel.

JAY RAYMOND LEVINSON,
On the Brief.